Reading the tea leaves: Decoding China’s 2024 Two Sessions

China's Two Sessions (Lianghui) refer to the annual plenary sessions of the country's two major political bodies, the National People's Congress (NPC) and the Chinese People's Political Consultative Conference (CPPCC). During the Two Sessions this year, Chinese Premier Li Qiang delivered his first Government Work Report (the Report). The Report offers an economic blueprint that provides businesses and investors with first-hand insights into the thinking of China's policymakers and their priorities for the coming year. This year's Two Sessions have been closely watched for any signs of major government policy to support growth and navigate the ongoing economic transformation.

The Report also offers a glimpse into China's industrial policy that will have a significant bearing on both state and private investment.

In our China Economic Quarterly Q4 2023 (CEQ Q4), we analysed China's economic data for 2023 and developed our views on China's outlook for 2024 in the areas of GDP, the property sector, a pivot towards high-tech sectors, domestic consumption, as well as foreign trade and policy stimulus. The Report touched on most of these areas that we covered. In this review, we build upon our CEQ Q4 analysis to decode the key policy messages from this year's Two Sessions.

Economic growth target

> A comprehensive analysis and assessment shows that China's development environment this year will continue to feature both strategic opportunities and challenges with favourable conditions outweighing unfavourable ones."[1]

Premier Li Qiang announced China's GDP growth target of around 5% for 2024, along with a series of detailed economic development targets ranging from the unemployment rate and CPI to balance of payments and energy consumption. China's GDP expanded by 5.2% in 2023 thanks to the economic recovery fuelled by the lifting of pandemic restrictions as well as a lower base the previous year. In the absence of a favourable base effect, the growth target for 2024 seems ambitious, but signals policymakers' confidence in the country's economic outlook and their will to shore up the economy with policy support.

The Premier highlighted China's vast consumer market, its complete industrial eco-system, and huge skilled labour force as the tailwinds to propel economic growth. Accordingly, the Report shows that policymakers have formulated their economic policies around these strengths, from upgrading China's industrial system and pushing into high-tech sectors to expanding domestic demand. The success of these policies will be critical for overcoming both the structural and geopolitical challenges faced by the Chinese economy.

1. Citations are from the Report on the Work of the Government delivered at the Second Session of the 14th National People's Congress of the People's Republic of China on 5 March 2024.

The official growth target has also reinforced the view that China's economy is entering a new phase of slower, but more sustainable and balanced growth. Given the sheer size of China's economy, it wouldn't be reasonable to expect the robust economic growth that China experienced over the last three decades to continue. The GDP target, along with the list of government work priorities from the Report, indicates that rebalancing the economy towards a growth model driven by innovation and consumption is top of mind for policymakers. To navigate the transformation, the Report outlined a multi-pronged approach to the economy, including fiscal and monetary policy aimed at stabilising growth, doubling down on technological innovation and institutional reforms to spur productivity, as well as policy support for domestic consumption, while containing risks in the property sector and local debts. We will focus our analysis of the Report around these four areas.

Development targets

- **GDP**: around 5%
- **New urban jobs**: over 12 million
- **Unemployment rate**: around 5.5%
- **CPI**: around 3%
- **Personal income growth**: in step with economic growth
- A basic equilibrium in **balance of payments**
- **Energy consumption** per unit of GDP: around -2.5%

Fiscal and monetary policy

> We should intensify counter and cross cyclical adjustments through macro policies, continue to implement a proactive fiscal policy and a prudent monetary policy, and strengthen coordination between policy instruments while developing new ones."

To clarify the goal of China's economic policy, the Report reiterated a key message from the Central Economic Work Conference held in December 2023 - China will adhere to the principles of "pursuing progress while ensuring stability, promoting stability through progress, and establishing the new before abolishing the old". While the Chinese government has long placed emphasis on stability, "promoting stability through progress" and "establishing the new before abolishing the old" are newly introduced catchphrases, signalling policymakers are ready to roll out additional policy measures to stabilise the economy if growth slows significantly or real estate debt risk spreads further.

More specifically, the Report outlined fiscal and monetary tools that policymakers will deploy to help the economy hit their growth target. Fiscal policy will be expansionary, with a fiscal budget deficit of 3% of GDP that represents an increase of RMB180 billion. Public expenditures have been budgeted to grow by RMB1.1 trillion to RMB28.5 trillion. Additionally, local governments will be allowed to issue RMB3.9 trillion of special bonds, marking an increase of RMB100 billion. Aligned with the country's focus on high quality growth, the Report revealed upcoming "structural tax and fee reduction policies" with priority given to the technology and manufacturing sectors. It is noteworthy that the government raised its deficit target from an initial 3% to 3.8% in 2023, suggesting policymakers have both the will and tools to further scale up fiscal stimulus when they deem additional support for the economy is necessary to meet the official growth target.

Most notably, to fund strategic development and national security projects, the Report revealed a plan to issue RMB1 trillion of ultra-long special central government bonds this year and implies that the government will continue to do so in the next few years. This marks the first such sale since 2020 when the government issued special bonds to fund pandemic relief spending. This move indicates a shift in the fiscal stimulus approach at a time when local governments grapple with a slowing property sector and ballooning debts - the central government is willing to deploy its robust balance sheet to shore up the economy.

Monetary policy will remain accommodative. The Premier pledged to ensure sufficient money supply to achieve GDP growth and CPI targets, while continuing to reduce financing costs and support micro, small and medium enterprises. The Report's mention of improving the "monetary policy transmission mechanism" signals upcoming cuts to rates and banks' reserve ratio throughout the year. Further, the Report reiterated the goal of keeping RMB stable, suggesting the PBOC will strike a delicate balancing act between supporting growth through rate cuts and keeping the currency from depreciating further against the U.S. dollar.

Proactive fiscal policy

- Deficit to GDP: 3%
- Government deficit: 4.06 trillion (+180 billion)
- Public expenditure: 28.5 trillion (+1.1 trillion)
- Special purpose bonds: 3.9 trillion (+100 billion)
- Ultra-long special treasury bonds: 1 trillion
- Transfer payments to local governments
- Tax and fee reduction

- Adequate liquidity
- Aggregate financing and money supply in step with economic growth and CPI
- Lower financing costs
- Monetary policy transmission mechanism
- Stable RMB
- Support for micro, small and medium enterprises

Prudent monetary policy

New quality productive forces

> “We should give full rein to the leading role of innovation, spur industrial innovation by making innovations in science and technology and press ahead with new industrialisation, so as to raise total factor productivity, steadily foster new growth drivers and strengths, and promote a new leap forward in the productive forces.”

Technology and innovation remain the overarching theme of this year’s Two Sessions. “New quality productive forces”, a new concept emphasised in the Report, points to China’s productivity imperative through high-tech, high-efficiency and high-quality development. The concept epitomises China’s renewed push for high quality growth through long-term investment in scientific breakthroughs and high-tech sectors with a near-term effort to upgrade China’s industrial system through digitalisation. From an economic perspective, the emphasis on the concept also represents the government’s recognition of the limits of China’s previous growth model that relied on debt-fuelled investment in the real estate sector and signals a shift towards productivity as the new driver of China’s economic growth. Boosting the country’s total factor productivity through technology and innovation also represents a policy response to the structural challenges of diminishing returns to investment and a shrinking labour force.

The Report outlined near-term and long-term policies to develop new productive forces. In the near-term, digital transformation remains a major source of productivity gain. Elaborating on this policy, the National Development and Reform Commission (NDRC) highlighted Data Element X, a joint government initiative recently introduced by seventeen Chinese government departments and agencies. The plan aims to grow China’s data industry by over 20% through the end of 2026, by unlocking the value of data as a new productive factor. The NDRC pledged to improve the quality of data supply, circulation mechanisms, and data application, including removing data barriers to promote innovation in intelligent connected vehicles and training large-scale AI models. In particular, the plan has identified 12 sectors that are high on policymakers’ digitalisation agenda, ranging from industrial manufacturing and transportation to financial services and healthcare. To achieve the goals, the government encourages data firms to go public and raise capital from diverse funding sources.

Long-term, the Report reveals policy support intended for the country to leap ahead in emerging and future industries such as new materials, biomanufacturing and quantum technology, while doubling down on strategic sectors where China already leads such as new energy vehicles. The Report also highlighted investment opportunities for venture capital and equity investment, as the Premier pledged to encourage their development while improving the functions of industrial investment funds to support these industries. The NDRC, the top economic planner, also revealed policymakers' regional focus for developing high-tech industries. The government will encourage technological innovation industries in the Beijing-Tianjin-Hebei region, the Yangtze River Delta, and the Greater Bay Area, plan coordinated development of China's future industries in the Yangtze River Delta, build advanced manufacturing clusters in the central and eastern region, and promote new materials, new energy and equipment manufacturing in the country's western region.

Digital economy (Data X)

- Intelligent manufacturing
- Modern agriculture
- Commercial circulation
- Transportation and logistics
- Financial services
- Technological innovation
- Cultural tourism
- Emergency management
- Meteorological service
- Urban governance
- Healthcare
- Green and low-carbon

Emerging and future industries

- New energy vehicles
- New materials
- Innovative drugs
- Biomanufacturing
- Commercial spaceflight
- Low altitude economy
- Quantum technology
- Life sciences
- AI
- Hydrogen
- Nuclear fusion

1 x 2 x 3

Integrated development of tech industries and joint research on core technologies

2

Formulate coordinated development plan for emerging and future industries

4

Advanced manufacturing clusters

5

New materials, new energy, and equipment manufacturing

Institutional reform

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We will press ahead with critical reform tasks in key areas and at crucial links. We will see that the market plays the decisive role in the allocation of resources and the government better fulfils its role. We will foster a world class business environment that is market oriented, law based, and internationalised and strive to build a high standard socialist market economy.”

The Report stressed policymakers’ support for both SOEs and private firms. Reform initiatives will involve getting SOEs to “improve their core businesses, enhance their core functions, and increase their core competitiveness.” The Report revealed there are also policy measures aimed at addressing challenges faced by private firms regarding “market access, access to factors of production, impartial law enforcement, and protection of rights and interests.” In particular, the government pledged to direct an increasing share of financial capital to the private sector through loans and bonds.

To achieve this goal, the government pledged to let the market play a greater role in the allocation of resources, tapping into another source of productivity gains for the economy. Compared to SOEs, the private sector has faced higher hurdles in accessing bank credit. As a result, government-led investment has been growing at a quicker pace than private investment. For example, in January-February this year, private investment returned to positive territory and eked out a 0.4% gain, yet it remains well below the country’s overall growth for fixed asset investment of 4.2%. The trend demonstrates that institutional reform remains another major source for productivity gain within the Chinese economy.

Concurrently, emphasis on easing access to bank credit for private firms echoes the government’s recent policy initiatives that support China’s private economy. In November 2023, the PBOC along with seven other Chinese ministries unveiled 25 detailed measures aimed at bolstering private sector investment by directing financial capital to private firms, particularly in the technology and innovation sector. The emphasis on private firms’ financing in the Report suggests government agencies will likely accelerate the implementation of these measures in the coming year.

Financial support measures to boost development and growth of the private economy

Bank loans

- Increase the proportion of private sector loans by setting annual service targets in performance assessment
- Increase support for first-time and unsecured borrowers
- Key sectors: sci-tech innovation, “specialised, sophisticated, distinctive and innovative” enterprises (专精特新), green and low carbon industry, industrial foundation reengineering projects, SMEs

Capital market

- Improve the registration system for debt financing instruments
- Encourage institutional investors to invest in bonds issued by private enterprises
- Support private enterprises to conduct public offerings, M&As, and reorganisations
- Empower regional equity markets and equity investment funds to boost equity financing in high-quality private enterprises

Foreign exchange

- Introduce additional foreign exchange facilitation policies and services to help private enterprises expand globally and attract global capital.
- Facilitate payments and receipts under the current account
- Optimise cross-border investment and financing facilitation policies
- Enhance the special foreign exchange services for cross-border finance

Policy implementation

- Comprehensive use of monetary policy tools, fiscal incentives and subsidies, as well as insurance protection to motivate financial institutions to support the private economy
- Enhance collaboration between the government departments supporting policies and making relevant arrangements

Domestic demand

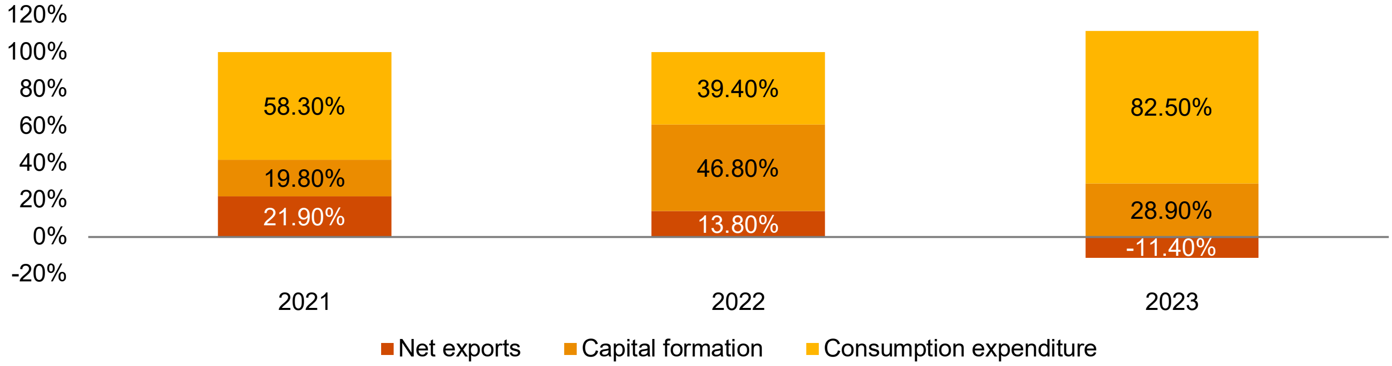
> We will integrate the strategy of expanding domestic demand with efforts to deepen supply side structural reform and better coordinate consumption and investment, so as to more effectively drive economic growth."

Domestic demand is high on the policy agenda, ranking in the third-place on the government's list of major tasks for 2024, only after science and technology development. The Report signals upcoming policy support to boost consumer spending on new-energy vehicles, electronic products, and other big-ticket items through trade-in programs, as well as consumption related to smart homes and domestic brands. Domestic demand is playing an increasingly prominent role in China's economic growth. According to the National Bureau of Statistics of China, domestic demand contributed 111.4% to China's GDP growth in 2023, while final consumption added 4.3 percentage points to the economic growth and accounted for 82.5% of China's total GDP growth. Nevertheless, retail sales and CPI data consistently point to a softer-than expected recovery in consumer demand. As such, the government will likely continue to roll out policy measures to revive consumer spending while growing household income.

The government will also promote digital, environmentally friendly and health-related consumption, and encourage consumer spending on services including entertainment, tourism, and sports events. In addition, the Report mentioned government support for private entities to provide community services and upgrade elderly care, childcare and housekeeping services. In recent years, a new shift in consumer spending patterns has been taking root. As service consumption continues to gain momentum, the service portion of the per capita consumption expenditure has risen from 39.7% in 2013 to 45.2% in 2023. During the Chinese New Year holidays this year, Chinese tourists made 474 million trips, marking a 19% increase from 2019, while total expenditure surpassed the 2019 level by 7.7%.

At the same time, aligned with fiscal policy and supportive measures for the private sector, the government also plans to boost investment through government spending and public-private partnerships in mega projects. Additionally, the government has signalled there will be support for firms to upgrade production and service equipment.

Contribution of each component to GDP growth



Foreign trade and investment

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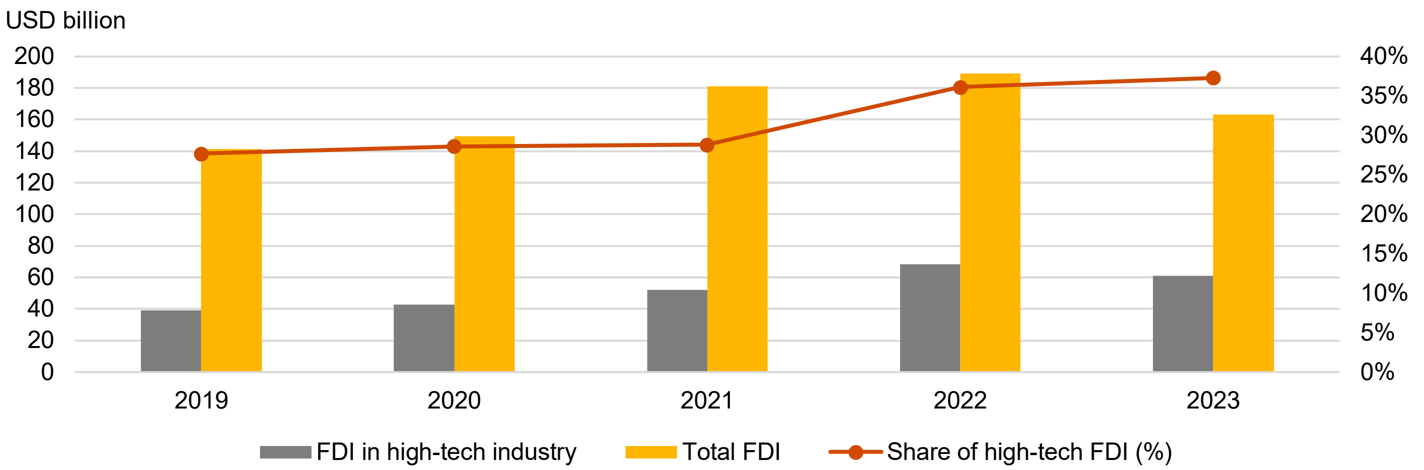
We will promote alignment with high standard international economic and trade rules, steadily expand institutional opening up and facilitate interplay between domestic and international markets. We will ensure the overall stable performance of foreign trade and foreign investment and foster new strengths in international economic cooperation and competition.”

Regarding foreign trade, the Premier highlighted China’s achievement in the “new three” exports (EVs, lithium-ion batteries, and solar panels) and pledged continued support for these sectors. China’s “new three” exports grew 29.9% in 2023, defying the decline of 4.6% in total exports. However, Chinese exporters face fraught overseas markets framed by sluggish consumer demand, sticky inflation, and rising geopolitical tensions. Also, protectionism is on the rise - the EU launched a probe into Chinese subsidies for electric vehicles. Going forward, concerns about China’s continued investment in advanced manufacturing might stoke a further backlash from its major trading partners.

The Report revealed policymakers’ plans for building other drivers of growth, with a focus on cross-border e-commerce and intermediate goods trade. The NDRC vowed to upgrade pilot free trade zones (FTZ) and the Hainan Free Trade Port. In particular, the economic planner intends to “implement both nationwide and pilot FTZ negative lists for cross-border trade in services” and “promote digital and green transformation of trade.” Aligned with these focal points, China’s trade within ASEAN will likely remain a bright spot in the years to come. ASEAN is already China’s largest trading partner, and the Premier pledged to push forward negotiations on the Version 3.0 China ASEAN Free Trade Area (FTA) and work towards joining the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Digital Economy Partnership Agreement (DEPA).

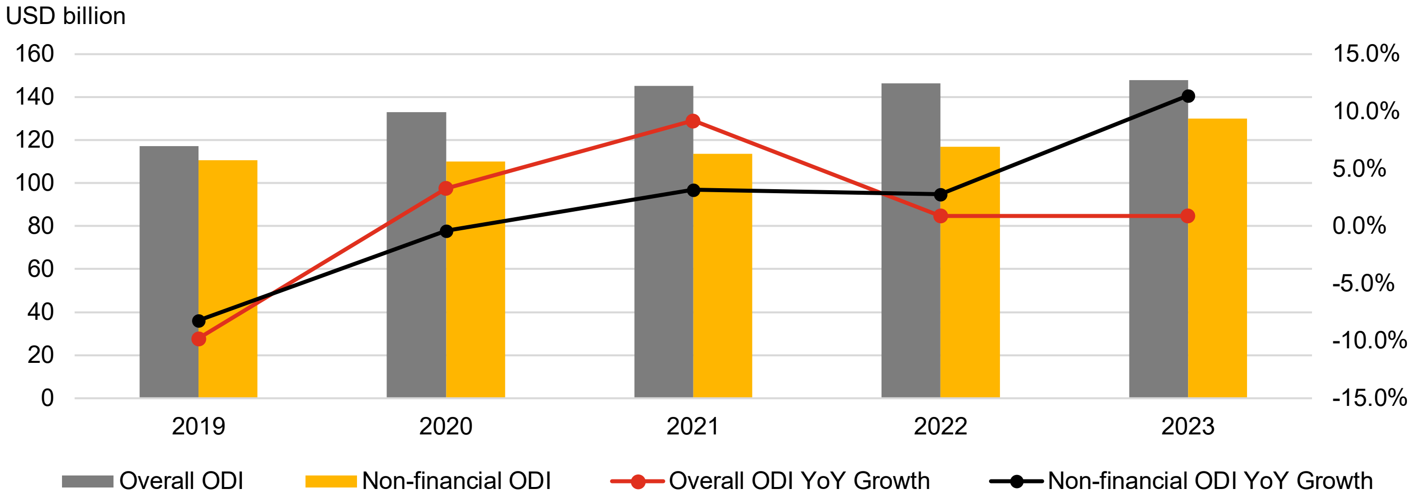
On foreign direct investment (FDI), the Premier announced that China will lift all market-access restrictions on foreign investment in the manufacturing sector, while opening up its services sectors including telecommunications and healthcare. Following the call, the State Council announced an action plan that outlines 24 measures aimed at easing market access and levelling the playing field to attract foreign investment. As part of the plan, the government will shorten its negative list for foreign investment and ease restrictions on data flows between foreign subsidiaries in China and their headquarters. Additionally, the plan hinted at policy support for foreign companies to invest in high-tech sectors and participate in national R&D programs. Although the ongoing restructuring of supply chains will likely continue in the near-term, China has managed to attract more FDI into high-tech sectors, while Chinese firms have also been pursuing outward FDI for global expansion.

High-tech foreign direct investment 2019-2023



Note: FDI data for 2023 is based on press release statistics
Source: Ministry of Commerce, PwC analysis

Outward direct investment 2019-2023



Note: ODI data for 2023 is based on press release statistics
Source: Ministry of Commerce, PwC analysis

Green and low-carbon development

"Acting on the principle that lucid waters and lush mountains are invaluable assets, we will make concerted efforts to cut carbon emissions, reduce pollution, pursue green development, and boost economic growth so as to build a Beautiful China featuring harmony between humanity and nature."

Aligned with the green and low-carbon development imperative, the Report set a target for reducing energy consumption per unit of GDP by about 2.5% in 2024. China's transition to a green and low-carbon economy involves environmental protection through improving air quality and water resources, and also includes building related industries and developing technologies. In 2023, China's newly installed renewable energy capacity matched the annual increase in domestic demand for electricity for the first time.

The transition also aligns with China's pivot towards high-tech sectors and investments into the EVs and renewable energy sectors. To further facilitate the process, the Report noted that the government will "improve fiscal, tax, financial, investment, and pricing policies in support of green development as well as relevant market-based mechanisms". While also noting efforts will be made to "encourage the R&D and application of advanced energy-saving and carbon reducing technologies and accelerate the development of green and low-carbon supply chains." Further, the Beautiful China Initiative, a policy program that includes a detailed timeline for achieving carbon peak and neutrality, is expected gain further momentum this year, as the Report hinted at policy measures to improve carbon accounting and verification, as well as expanding the national carbon market to cover more sectors.

Property sector and local debts

> We will continue to ensure greater security through high quality development and promote high quality development with a greater degree of security. We will defuse risks in real estate, local government debt, and small and medium financial institutions by addressing both symptoms and root causes. By doing so, we will safeguard overall economic and financial stability.”

The Report highlighted the real estate sector and local debts as the main risks for policymakers to tackle. Consistent with the government’s recent whitelist financing program, the Report reiterated equal treatment for state-owned and private home builders. Also, government-subsidised housing will be scaled up. Finally, the government pledged to “implement a package of measures to defuse risks caused by existing debts and guard against risks arising from new debts.”

As the government works to wean the Chinese economy off its reliance on real estate investment and push towards a growth model led by innovation and consumption, a protracted property downturn has put strains on local governments’ finances and exacerbated the debt burden for Chinese developers. The Report’s emphasis on defusing risks represents the government’s recognition of the challenges and signals policymakers’ willingness to put a floor under the property market. This is also aligned with the government’s pledge to “promoting stability through progress” and “establishing the new before abolishing the old.” As such, the government will likely continue to push banks to lend to developers through policy measures such as the whitelist program, while further relaxing restrictions on home purchases.

Conclusion

This year’s Two Sessions set the stage for China’s next phase of growth. In this report, our analysis decoded the key messages from the Two Sessions. As the Chinese economy shifts gear towards a more balanced and sustainable growth model, the Government Work Report revealed policymakers’ multi-pronged strategy to develop new quality productive forces while ensuring stability. Technology and innovation will remain the overarching theme, along with institutional reforms to unlock the productivity of the private sector and further opening-up of the market for foreign investors. This Government Work Report presented new opportunities for growth. Businesses and investors should ride the policy wave.

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